

A "service exchange" program is taxed under the Retailers' Occupation Tax Act or the Service Occupation Tax Act depending upon the relationship between the parties. See 86 Ill. Adm. Code 130.2015. (This is a GIL.)

April 20, 2006

Dear Xxxxx:

This letter is in response to your letter dated January 25, 2006, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

I am writing you today for an official ruling on the proper collection of sales tax for the circumstances I am going to describe.

I am a bowling center in Illinois who owns a System. From time to time the components of that system go bad. ABC offers an Electronic Repair Service. The service works as follows. When a part goes bad you ship the bad part to ABC Electronic Repair with a description of the problem. They repair the part or send you a repaired part in return. They never return your original part back. Sometimes you may get your part back or you may get a repaired part that they inventory. You never get a new part. The issue is that ABC is charging sales tax on 100% of the bill. When you read section 140.101 of your regulations it clearly states that in a situation like I am describing you would charge 50% of the sales tax. I have enclosed copies of some of my invoices to serve as examples of how they are billing me. Please send me a ruling so that I can show it to ABC so that they begin applying this tax correctly.

DEPARTMENT'S RESPONSE:

A "service exchange" program, as described in your letter, is taxed under the Retailers' Occupation Tax Act or the Service Occupation Tax Act depending upon the relationship between the parties. The nature of the relationship usually depends upon the agreement between the two parties. However, the actual transaction occurring between the parties may also determine how the program

is taxed. Generally, how a repairman's sales are taxed depends on whether or not he or she has agreed to send the customer's actual equipment or components back to that customer.

Basically, if a repairman has not agreed to send the customer's equipment or components back to that specific customer, and if the repairman rebuilds, repairs, or reconditions a piece of equipment or component that belongs to him and sells that equipment or component to a different customer as a recycled or reconditioned piece of equipment or component, the repairman is acting as a retailer and is subject to Retailers' Occupation Tax liability. Therefore Retailers' Occupation Tax and Use Tax liability would be incurred on 100% of the purchase price of the equipment. See 86 Ill. Adm. Code 130.2015.

On the other hand, if a repairman (serviceman) has agreed to send the customer's equipment or component back to that specific customer, the repairman is not acting as a retailer but instead is acting as a serviceman repairing and reconditioning that customer's equipment or components of that equipment. Consequently, the serviceman would incur Service Occupation Tax or Use Tax liability depending on how the serviceman calculates his tax base.

A serviceman's liability may be calculated in one of four ways:

1. Separately stated selling price of tangible personal property transferred incident to service;
2. 50% of the serviceman's entire bill;
3. Service Occupation Tax on the serviceman's cost price if he is a registered de minimis serviceman; or
4. Use Tax on the serviceman's cost price if he is a de minimis serviceman not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale price of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the serviceman's cost price of the tangible personal property transferred. See 86 Ill. Adm. Code 140.106. These methods result in the customer incurring a Service Use Tax liability. See 86 Ill. Adm. Code 160.101.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See 86 Ill. Adm. Code 140.109. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred incident to the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction-by-transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the

Service Occupation Tax rates for their locations. This method also results in the customer incurring a Service Use Tax liability.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See 86 Ill. Adm. Code 140.108. Under this method the customer incurs no Service Tax liability.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Edwin E. Boggess
Associate Counsel

EEB:msk